Petition

81-988

No. .....

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In the Supreme Court of the United States

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COMMODORE BUSINESS MACHINES INC.
COMMODORE BUSINESS MACHINES (CANADA) LIMITED,
Petitioners,

VS.

MCDONNELL DOUGLAS CORPORATION,
Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

JOHN W. CLARK
Professional Law Corporation
99 Almaden Boulevard, Suite 850
San Jose, California 95115
Counsel for Petitioners

BORG PRINTING COMPANY OF CALIFORNIA, 346 FIRST STREET, SAN FRANCISCO 94105

QUESTIONS PRESENTED

1. Whether due process and 28 U.S.C. 636(b) require hearing before the District Court, where the District Judge rejects the Magistrate's proposed findings on credibility and those findings are dispositive.

2. Whether Petitioners' due process and statutory rights were violated when the District Court, without making a *de novo* determination of the Magistrate's initial report and without issuing instructions, remanded the case to the United States Magistrate for revised findings.

3. Whether Petitioners' due process and statutory rights were violated by the District Court's rejection of the initial findings of the United States Magistrate, without additional evidence or hearing and without hearing or seeing the witnesses presented at trial.

Petitioners are wholly owned subsidiaries of Commodore International, Ltd., a Bahamian corporation.

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No. .....

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COMMODORE BUSINESS MACHINES INC.
COMMODORE BUSINESS MACHINES (CANADA) LIMITED,
Petitioners,

VS.

McDONNELL DOUGLAS CORPORATION,
Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

Petitioners COMMODORE BUSINESS MACHINES, INC. and COMMODORE BUSINESS MACHINES (CANADA) LIMITED respectfully pray that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this proceeding on August 31, 1981.

OPINIONS BELOW

The August 31, 1981 opinion of the Court of Appeals, whose judgment is herein sought to be reviewed, is not yet reported and is reprinted in the appendix to this petition, pages 1-9. The August 10, 1979 findings of fact, conclusions

of law and order upon objections to Magistrate's recommendation rendered by the District Court for the Northern District of California is reprinted in the appendix pages 10-19.

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was entered August 31, 1981. This petition for certiorari is filed within ninety days of that date. Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

This case involves the due process clause of the Fifth Amendment to the Constitution of the United States, which provides:

> "No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, *nor be deprived of life, liberty, or property, without due process of law;* nor shall private property be taken for public use, without just compensation." (Emphasis added)

This case also involves Title 28 United States Code § 636.

STATEMENT OF THE CASE

This is a diversity action brought by McDonnell Douglas Corporation pursuant to 28 U.S.C. § 1332.

On February 22, 1978 McDonnell Douglas brought an action for breach of contract against Commodore, claiming $432,908.36 for goods sold and delivered to Commodore

between July 1, 1976 and August 15, 1977. Commodore claimed credit of $261,000.42 for defective goods shipped to Commodore prior to July 1, 1976.

On March 22, 1979, the parties entered into a stipulation waiving their right to trial before a United States District Judge and consenting to trial before U.S. Magistrate Frederick J. Woelflen.

On March 28, 1979, trial was held before the U. S. Magistrate pursuant to stipulation. Evidence was presented, and the case submitted

On April 19, 1979, the U. S. Magistrate filed his trial report and recommendations and found Commodore entitled to the claimed credit of $261,000.42, leaving a balance owing from Commodore to McDonnell Douglas of $171,907.94.

Thereafter, McDonnell Douglas filed its motion in the District Court objecting to the proposed findings of fact, conclusions of law and report, with a supporting memorandum and supplementary memorandum. On or about May 15, 1979, Commodore filed its memorandum in opposition.

On June 7, 1979, without making a *de novo* determination of the case, without a hearing, and without specific instructions, the District Court entered its "Order of Remand", directing the magistrate to prepare "revised" proposed findings of fact, conclusions of law and report.

Thereafter, on July 10, 1979, without further hearing or any additional evidence, the U.S. Magistrate filed his revised report, findings of fact, conclusions of law and recommendations, and found Commodore was not entitled to the credit of $261,000.42, and owed McDonnell Douglas the full sum of $432,908.36.

On July 20, 1979, Commodore filed its motion objecting to the Magistrate's revised report. McDonnell Douglas filed its memoradum in opposition. Hearing was held before the

District Court on August 10, 1979, at which time the District Judge denied Commodore's motion, and said:

> "I think the best one can say about your case is that it could be construed either way." (C.Rt.II, 7.)

The District Judge at no time heard or saw any of the witnesses presented at the trial before the United States Magistrate.

On August 10, 1979, the District Judge filed his findings of fact, conclusions of law and order, finding McDonnell Douglas entitled to the full sum of $432,908.36. The District Judge indicated that only *after* the revised report had he made a *de novo* determination of the proceedings based upon transcripts of the record and written memoranda filed and served in the action. Judgment was filed the same day.

The proceedings in the District Court show the following sequence of events: the parties stipulated to a trial before the United States Magistrate; trial was held and the Magistrate found Commodore entitled to the offset claimed; written objections were filed in the District Court to the Magistrate's initial report by McDonnell Douglas; the District Judge, without making a *de novo* determination, and without issuing specific instructions, remanded the case to the U. S. Magistrate for a revised report; without further hearing or additional evidence, the U. S. Magistrate filed a revised report directly contrary to his initial report and found in favor of McDonnell Douglas on the issue of the offset; Commodore then filed its objections in the District Court to the Magistrate's revised report; only then did the District Judge make a *de novo* determination based solely upon the transcripts of the prior proceedings, the District Judge not seeing or hearing any of the witnesses; the District Judge then filed his findings of fact and conclusions of law in conformity with the Magistrate's revised findings,

directly contrary to the Magistrate's initial findings, and entered judgment in favor of McDonnell Douglas for the full sum claimed.

Notice of appeal was timely filed September 10, 1979.

On August 31, 1981, the United States Court of Appeals for the Ninth Circuit affirmed the judgment of the District Court, holding that the actions of the District Court complied with 28 U.S.C. § 636(b), the Magistrate's Act. The Court of Appeals specifically held that the District Court was not obliged to hear or see any witnesses and was entitled to make a *de novo* determination solely upon the transcripts of the prior proceedings and that the District Judge used a correct standard of review in his *de novo* determination of the Magistrate's revised findings.

REASONS FOR GRANTING THE WRIT

Certiorari Should Be Granted (1) to Construe 28 U.S.C. § 636(b) in a Case Where a Magistrate's proposed Findings on Credibility Are Rejected by the District Court (a Question Expressly Reserved by This Court in U.S. v. Raddatz, 447 U.S. 667 (1980)); and (2) to Afford Petitioners Their Due Process and Statutory Rights.

The issue in this case is whether the judgment entered by the District Court complies with the due process requirements of the Fifth Amendment of the United States Constitution and with the statutory provisions embodied in 28 U.S.C. § 636, the Magistrate's Act.

It is well established law that, to satisfy both constitutional and statutory requirements, the District Court is required to make a *de novo* determination when objections are filed to a report issued by a United States Magistrate. This Court confirmed that principle recently in *United States v. Raddatz*, 447 U.S. 667, 65 L.Ed.2d 424 (1980). This Court noted that after a Magistrate files his proposed findings and recommendations, any party may file objections within ten days and that "the statute then provides: 'a judge of the court shall make a *de novo* determination of those

portions of the report or specified proposed findings or recommendations to which objection is made. A judge of the court may accept, reject, or modify, in whole or in part, the findings or recommendations made by the Magistrate. The judge may also receive further evidence or recommit the matter to the Magistrate with instructions.' § 636(b)(1). It should be clear that on these dispositive motions, the statute calls for a *de novo* determination . . ." *Id.* at 673-74.

The requirement of a *de novo* determination has been specifically addressed by the Court of Appeal in the case of *Muhich v. Allen*, 603 F.2d 1247, (7th Cir. 1979):

> "Under section 636(b)(1)(C), the District Court is *required* to conduct a *de novo* determination where objections to the magistrate's report have been filed by the parties with the District Court." *Id.* at 1252. (Emphasis added)

The statutory requirement was simply ignored by the District Court. The Magistrate filed his trial report and recommendations April 19, 1979. McDonnell Douglas filed its objections and, on June 7, 1979, the District Court ordered the case remanded to the United States Magistrate for preparation of revised findings. Remand was made without a *de novo* determination of the proceedings before the U.S. Magistrate. The remand contained no specific instructions.

Commodore was entitled to a *de novo* determination of McDonnell Douglas's objections to the initial findings of the Magistrate. By simply remanding the action without a *de novo* determination and without issuing specific instructions, the District Court forced Commodore to argue for rejection of the Magistrate's revised report, instead of merely assuming the lesser burden of urging affirmance of the Magistrate's initial report.

What the District Court in essence did was nullify completely the initial report of the Magistrate. Were this Court to allow the judgment below to stand, it would sanction the very abuse the Magistrate's Act seeks to avoid—disintegration of the integrity of the fact finding process.

To uphold the judgment would allow a district court to remand for revision a U.S. Magistrate's report without conducting a *de novo* determination, implicitly telling the U.S. Magistrate—without more—to change his initial report. After receiving the revised findings of the Magistrate, the District Court merely affirms the Magistrate's altered findings without a "*de novo* determination". This would render the initial Magistrate's report a nullity, and turn the "winning party" into a "losing party" without meeting the mandatory requirement of § 636(b)(1) which expressly provides that the district judge "*shall*" make a *de novo* determination of those portions of the Magistrate's report to which objection is made.

Had the District Court followed the statute and made a *de novo* determination, the District Court would have been obligated by the due process clause of the Fifth Amendment of the United States Constitution to see and hear the witnesses presented. Thus, the District Court's failure to make a *de novo* determination of the initial report of the Magistrate both violated the statute involved and directly led to violation of Petitioners' constitutional rights under the due process clause of the Fifth Amendment to the United States Constitution.

This Court, in *United States v. Raddatz, supra,* discussed at length the due process requirements required of a district court in making a *de novo* determination of a magistrate's report. This Court clearly held that when a district court *adopts* a magistrate's proposed result, it may do so without seeing or hearing the witnesses presented.

Just as clearly, the Court left open the determination of whether, in *rejecting* a magistrate's report based on the credibility of witnesses, a district judge is required to see and hear the witnesses presented. Specifically, in footnote 7 to the opinion in *Raddatz, supra,* this Court stated:

> "Neither the statute nor its legislative history reveals any specific consideration of the situation where a district judge after reviewing the record in the process of making a *de novo* determination has doubts concerning the credibility findings of the magistrate. *The issue is not before us, but we assume it is unlikely that a district court would reject a magistrate's proposed findings on credibility when those findings are dispositive and substitute the judge's own appraisal; to do so without seeing and hearing the witness or witnesses whose credibility is in question could well give rise to serious questions which we do not reach.*" (Emphasis added.)

Petitioners urge this Court that the present case offers the opportunity to reach the issue reserved in the *Raddatz* decision. Here, the District Court judgment is clearly based on credibility as the judge himself noted:

> "I think the best one can say about your case is that it could be construed either way." (C.Rt.II, 7.)

Therefore, a decision of this Court is necessary to afford guidance to the lower courts.

At least one court of appeal has already ruled on the issue raised in footnote 7 to the *Raddatz* decision. In *Louis v. Blackburn,* 630 F.2d 1105 (5th Cir. 1980), the court interpreted *Raddatz* as Petitioners herein urge:

> "An additional hearing before a district judge who agrees with the credibility determination of the magistrate, would do little, if anything to further protect the defendant's interests . . . These safeguards are no

Appendix A

McDONNELL DOUGLAS CORPORATION,
Appellee,

v.

COMMODORE BUSINESS MACHINES INC.
and Commodore Business Machines (Canada) Limited,
Appellants.

No. 79-4616.

United States Court of Appeals,
Ninth Circuit.

Argued and Submitted May 13, 1981.

Decided Aug. 31, 1981.

Defendant appealed from a judgment of the United States District Court for the Northern District of California, William W Schwarzer, J., in favor of plaintiff in a breach of contract action. The Court of Appeals, Poole, Circuit Judge, held that: (1) parties' stipulation waiving trial by District Court and consenting to trial by United States magistrate did not deprive the District Court of the power to review the findings and recommendations of the magistrate, regardless of whether the stipulation could be read as intending such effect; (2) District Court was not required to hear all of the evidence before remanding case to magistrate for reconsideration; and (3) District Court acted within the mandate of the Magistrates' Act concerning review of magistrates' reports, when it remanded case to magistrate for reconsideration.

Affirmed.

1. United States Magistrates—5

Parties' stipulation waiving trial to the district court and consenting to trial by a United States magistrate did not deprive the district court of the power to review the findings and recommendations of the magistrate, regardless of whether the stipulation could be read as intending such effect. 28 U.S.C.A. § 636.

2. United States Magistrates—5

District court was not required to hear all of the evidence before remanding case to magistrate for reconsideration.

3. United States Magistrates—5

District court acted within the mandate of Magistrates' Act concerning review of magistrates' reports, when it remanded case to magistrate for reconsideration. 28 U.S.C.A. § 636(b).

Appeal from the United States District Court for the Northern District of California.

Before GOODWIN and POOLE, Circuit Judges, and WYATT,* District Judge.

POOLE, Circuit Judge:

Commodore Business Machines (Commodore) appeals the judgment of the United States District Court for the Northern District of California, awarding plaintiff McDonnell Douglas the full $432,000 claimed in its breach of contract action, and denying Commodore's claim for a set off in the amount of $261,000. Commodore does not contest its liability for the balance of the debt.

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*Honorable Inzer B. Wyatt, Senior United States District Judge for the District of New York, sitting by designation.

The dispute arose out of a contract between subsidiaries of the two parties. McDonnell Douglas' subsidiary, Nitron, supplied Commodore with semiconductors for use in electric calculators. The product supplied by Nitron was a wafer containing a number of individual chips. When Commodore received the wafers it sent them to Electronic Arrays, a subcontractor, where the wafers were tested and diced and the individual chips were packaged. The $261,000 at issue is the value of the approximately 319,000 chips that were rejected as defective during the Electronic Arrays packaging process from February, 1975 through June, 1976.

Commodore introduced evidence that several months after the chips were rejected in its testing process, Commodore presented a debit memorandum for their value to Nitron. Commodore's then president testified that Nitron's executives requested that Commodore withdraw the memorandum because its adverse effect on Nitron's profit reports would likely induce McDonnell Douglas to cause Nitron to retire from the production of chips. Commodore had an interest in Nitron's continued participation in this industry because Nitron was its only supplier. For this reason, Commodore agreed to withdraw the memorandum. There was apparently some discussion about reconsidering the memorandum when Nitron was in better financial condition. However, Commodore does not contend that any representative of Nitron ever expressly stated that Commodore was entitled to any specific amount of credit. The matter appears to have been left for later agreement. Commodore contends that Nitron's failure to object at this time to the amount of the credit claimed constituted some sort of assent to liability in that amount. McDonnell Douglas later sold Nitron and disavowed any credit to Commodore for defective chips.

Pursuant to the parties' stipulation waiving the right to trial by the court and consenting to trial before a magistrate, the case was referred to U.S. Magistrate Frederick J. Woelflen. At trial, Commodore based its claim for a set off to its contract liability on two theories: (1) that the goods rejected during the testing by Electronic Arrays were defective and therefore in breach of the contract warranty; and (2) that representatives of the parties agreed that Commodore would be entitled to set off $261,000 against sums due for future deliveries.

The magistrate issued his first report on April 19, 1979. He found that the rejected dice had latent process defects, as required to trigger the warranty clause, and hence were in breach of the contract. He concluded that Commodore was liable to McDonnell Douglas in the amount of $432,000, subject to a set off in the amount of $261,000.

McDonnell Douglas brought objections to this conclusion before the district court. Without further hearing and without stating any reasons beyond "good cause," that court remanded the case to the magistrate for revised findings and conclusions.

In his second report, the magistrate revised his earlier conclusion, holding (1) that Commodore had presented no evidence that Nitron had admitted that Commodore was entitled to a $261,000 credit, and (2) that Commodore had not satisfied its burden of proof as to the amount of the set off it claimed because there was no evidence showing that all of the rejected dice were latently defective. He therefore ruled that Commodore was liable for the full amount due under the contract, without set off.

Commodore brought objections to the district court, and that court issued its own opinion in this case. Regarding the breach of warranty theory, the district court deter-

mined that Commodore had failed to make an effective rejection of the dice because several months elapsed between their delivery and presentation of the credit memorandum. Under the UCC, therefore, Commodore bore the burden of proof as to whether there had been a breach of warranty, and had failed to carry that burden. The only evidence supporting Commodore's position was the list of rejects from the Electronic Arrays testing, but testimony showed that those defects could have accrued after production. There was no evidence establishing which, if any, of the rejected dice suffered from latent process defects. On Commodore's second theory, the court again reviewed the evidence, which very clearly showed that no agreement was ever reached as to the amount of credit, if any, to which Commodore was entitled. In view of these findings, the court entered judgment against Commodore for the full $432,000.

I

Commodore argues that the parties' stipulation waiving trial to the district court and consenting to trial by a United States magistrate had the effect of depriving the district court of the power to review the findings and recommendations of the magistrate. This theory must be rejected. In the first place, we seriously doubt that the form stipulation signed by the parties[1] could reasonably be read as intending the extraordinary effect of ousting

1. The stipulation form provided by the Northern District of California reads as follows:

> The undersigned counsel being fully aware of the right to trial of the captioned proceeding before a Judge of the United States District Court for this District, and in behalf of their clients, do hereby specifically waive trial before the District Judge and consent to jury..... court ..xx.. trial before United States Magistrate Frederick J. Woelfien.

the district court of its power to review the magistrate's report. See also N.D.Cal.Loc.R. 405(k) and 410—2(b).

More importantly, however, Commodore's claim is defective because it ascribes to the magistrate powers that he simply does not have. In 1976, Congress amended the Federal Magistrate Act, 28 U.S.C. § 631 *et seq.* Sections 636(a) and (b) describe the powers of magistrates.[2] Neither of

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2. The relevant portions of the statute are:

§ 636. Jurisdiction, powers, and temporary assignment.

(a) Each United States magistrate serving under this chapter shall have within the territorial jurisdiction prescribed by his appointment—

(1) all powers and duties conferred or imposed upon United States commissioners by law or by the Rules of Criminal Procedure for the United States District Courts;

(2) the power to administer oaths and affirmations, impose conditions of release under section 3146 of title 18, and take acknowledgments, affidavits, and depositions; and

(3) the power to conduct trials under section 3401, title 18, United States Code, in conformity with and subject to the limitations of that section.

(b)(1) Notwithstanding any provision of law to the contrary—

(A) a judge may designate a magistrate to hear and determine any pretrial matter pending before the court, except a motion for injunctive relief, for judgment on the pleadings, for summary judgment, to dismiss or quash an indictment or information made by the defendant, to suppress evidence in a criminal case, to dismiss or to permit maintenance of a class action, to dismiss for failure to state a claim upon which relief can be granted, and to involuntarily dismiss an action. A judge of the court may reconsider any pretrial matter under this subparagraph (A) where it has been shown that the magistrate's order is clearly erroneous or contrary to law.

(B) a judge may also designate a magistrate to conduct hearings, including evidentiary hearings, and to submit to a judge of the court proposed findings of fact and recommendations for the disposition, by a judge of the court, of any motion excepted in subparagraph (A), of applications for posttrial relief made by individuals convicted of criminal offenses and of prisoner petitions challenging conditions of confinement.

(C) the magistrate shall file his proposed findings and recommendations under subparagraph (B) with the court and a copy shall forthwith be mailed to all parties.

Within ten days after being served with a copy, any party may serve and file written objections to such proposed findings

these sections empowers magistrates to enter final judgments:

> In passing the 1976 amendments to the Federal Magistrates Act, Congress was alert to Art. III values concerning the vesting of decisionmaking power in magistrates. Accordingly, Congress made clear that the district court has plenary discretion whether to authorize a magistrate to hold an evidentiary hearing and that the magistrate acts subsidiary to and only in aid of the district court. Thereafter, the entire process takes place under the district court's total control and jurisdiction.

United States v. Raddatz, 447 U.S. 667, 681, 100 S.Ct. 2406, 2415, 65 L.Ed.2d 424 (1980) (footnotes omitted). *See also Mathews v. Weber*, 423 U.S. 261, 269-72, 96 S.Ct. 549, 553-55, 46 L.Ed.2d 483 (1976) ("A district judge would retain ultimate responsibility for decisionmaking in every instance in which a magistrate might exercise additional duties jurisdiction.")

[1] Thus, it is quite clear that any action taken by the magistrate was taken subject to the "inherent supervisory power of the district judge." *Harding v. Kurco, Inc.*, 603 F.2d 813, 814 (10th Cir. 1979). In reviewing the magistrate's report, the district judge did no more nor less than

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and recommendations as provided by rules of court. A judge of the court shall make a de novo determination of those portions of the report or specified proposed findings or recommendations to which objection is made. A judge of the court may accept, reject, or modify, in whole or in part, the findings or recommendations made by the magistrate. The judge may also receive further evidence or recommit the matter to the magistrate with instructions.

(3) A magistrate may be assigned such additional duties as are not inconsistent with the Constitution and laws of the United States.

fulfill his statutory and Constitutional responsibilities. And no agreement between the parties could have altered this state of affairs: the parties may not, by consent, invest greater powers in the magistrate than Congress has seen fit to vouchsafe him. *See Taylor v. Oxford,* 575 F.2d 152, 154-55 (7th Cir. 1978).

II

Commodore also contends that the district court's review of the magistrate's first report was defective because it was required to but did not hear all of the evidence itself before acting on the case. This argument is based on *United States v. Bergera,* 512 F.2d 391 (9th Cir.1975), in which the court held that protection of the integrity of the fact finding process requires that, before the district court may enter a judgment that disregards the recommendation of a magistrate who has heard all of the evidence, the district court must itself rehear all of that evidence. *Id.* at 393-94.

[2] Commodore maintains that *Bergera* governs this case because remand is tantamount to reversal. We cannot agree. The district court did not substitute its judgment for that of the magistrate on questions of witness credibility and weight of the evidence, and it did not adopt findings that differed from those presented by the magistrate. Rather, when it determined that the first report was deficient in some undisclosed respect, it called upon the magistrate who had heard the evidence to reconsider his conclusions. The integrity of the fact finding process was in no way implicated in this proceeding; indeed, the district court followed a course of action well calculated to protect it. It would be a most inefficient practice to compel a district court to hear all of the evidence itself before remanding to the magistrate, and we decline to mandate such a practice.

III

Finally, Commodore argues that the district court's review of the magistrate's first report was deficient because it applied an incorrect standard of review. Relying on Fed.R.Civ.P. 52(a), Commodore contends that the district court could not overturn the magistrate's original findings of fact unless they were clearly erroneous. This argument is without merit for reasons given above: the district court did not overturn the magistrate's findings of fact when it remanded the case for reconsideration.

[3] In any case, Fed.R.Civ.P. 52(a) does not state the standard of review that a district court must apply when it considers a magistrate's findings and recommendations. That standard is provided in the Magistrates Act, 28 U.S.C. § 636(b). Although the statute calls for application of the clearly erroneous standard when a district court reviews the magistrate's report on certain pretrial, non-dispositive motions, in all other cases, the statute grants the broadest possible discretion to the reviewing district court. When either party objects to any portion of the magistrate's report, the district court is charged to make a de novo determination of that portion. The court may "accept, reject, or modify, in whole or in part, the findings or recommendations made by the magistrate. The judge may also receive further evidence or recommit the matter to the magistrate with instructions." 28 U.S.C. § 636(b). There can be no doubt whatsoever that the district court in this case acted well within the mandate of this statute when it remanded the case for further consideration by the magistrate.

Commodore thus has presented no meritorious arguments for reversal of the judgment entered in this case. Accordingly, that judgment is AFFIRMED.

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AUG 10 1979

CLERK, U. S. DIST. COURT
SAN FRANCISCO

United States District Court
Northern District of California

No. C-78-0391-WWS

McDONNELL DOUGLAS CORPORATION,

Plaintiff,

v.

COMMODORE BUSINESS MACHINES, INC.
and COMMODORE BUSINESS MACHINES
(CANADA) LTD.,

Defendants.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER UPON OBJECTIONS TO MAGISTRATE'S RECOMMENDATION

Defendants have filed objections to the Magistrate's Revised Report, Findings of Fact, Conclusions of Law and Recommendations, which recommend that judgment be entered in favor of plaintiff in the sum of $432,908.36. The procedural history of this case is somewhat complex. Both parties consented to a court trial before U.S. Magistrate Frederick J. Woelflen on March 19, 1979. The trial was held on March 28, 1979. On April 19, 1979 the Magistrate filed a report recommending that judgment be entered in favor of plaintiff in the sum of only $171,907.94. That figure was obtained by allowing defendants to set off a

credit of $261,000.42 which they had claimed on account of the delivery of defective products by plaintiff. Plaintiff filed objections to the original report and this Court remanded the matter to the Magistrate for the preparation of revised recommendations on June 7, 1979. The revised report recommending that no setoff be allowed was filed by the Magistrate on July 10, whereupon defendants filed objections.

I. Procedural Objections

Defendants argue first that the above procedural history bars reconsideration and review of the magistrate's initial recommendation. They argue that their stipulation to a trial before the magistrate made his decision final and binding on this Court. The Local Rules, however, compel a contrary conclusion. Rule 410-2(b) provides that any party may file objections to a magistrate's findings and set them for hearing before the assigned judge. The Rule goes on to provide:

> The judge may determine the objections on the record before the magistrate or receive such additional evidence as he deems appropriate. The judge shall make a de novo determination of the matters to which objection is made and may accept, reject or modify the findings, recommendation or report, or remand the same to the magistrate.

Under these provisions, this Court's earlier remand and its instant *de novo* determination were proper and entirely consistent with the stipulated referral of the case to the magistrate for trial. See also 28 U.S.C. § 636(b)(1).[1]

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1. Defendants also object to the failure of plaintiff to notice a hearing when it filed its objections to the original magistrate's report. Although this may have been a technical violation of the local rules, it had no impact here. The judge has discretionary authority to decide issues without oral argument. Local Rule 220-I. That authority was exercised when this Court issued its

II. Substantive Objections

Turning to the merits, the only contested issue at this stage is whether defendants are entitled to a credit of $261,000.42 against the amount due plaintiff because of allegedly defective goods delivered under the contract. As noted above, the Local Rules permit the Court to make a *de novo* determination of this issue.

The controversy arises out of a contract between Nitron, a division of plaintiff McDonnell Douglas Corporation, and defendant Commodore Business Machines, Inc., a subsidiary of the other defendant Commodore Business Machines (Canada) Limited. Under this contract Nitron supplied Commodore with semiconductors for use in electronic calculators. The product supplied by Nitron was a wafer containing a number of individual chips. When Commodore received the wafers it sent them to Electronic Arrays, a subcontractor, where the wafers were tested and diced and the individual chips packaged. The $261,000.42 at issue here is the value of the approximately 319,000 chips which were rejected as defective during the Electronic Arrays packaging process from February, 1975 through June, 1976.

Plaintiff rested its case on admissions by defendants to the effect that Nitron had delivered and Commodore had accepted goods with a contract price of $432,908.36, which amount had not been paid. Plaintiff thus established its right to recover that amount from defendants, subject to any valid defenses.

Defendants' pleadings did not properly raise the issue of their entitlement to a credit or off-set. The answer con-

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order of remand to the magistrate. Defendants' written response to the objections was before the Court at the time the order was issued and thus defendants had an opportunity equal to plaintiff's to address the Court on this issue. No prejudice resulted from the technical failure to notice a hearing.

tained only a general denial; the credit was not pleaded either as an affirmative defense or counterclaim. At the start of the trial before the magistrate, however, plaintiff expressly consented to inclusion in the trial of the issue of defendants' entitlement to the $261,000.42 credit.[2] The failure to amend the answer does not prevent the Court from considering this issue now. Fed.R.Civ.P., Rule 15(b).

Defendants apparently rely on two separate theories to support their claim of an offset against the $432,908.36 which they concede is otherwise due plaintiff under the contract. The first theory is that plaintiff delivered products

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2. The reporter's transcript at page 4 reveals that Mr. Dunn, counsel for plaintiff, replied affirmatively to the following characterization of the issue before the court:

> THE COURT: The question was there was a transaction to sell a number of chips or so to the defendant for a given price, that there is a dispute as to a number of chips that allegedly were defective, and not in conformity with the contract and whether or not the defendant was entitled to some sort of an offset or credit for those particular items, and what the balance due on the contract is. I think that is what it gets down to, isn't it?
>
> MR. DUNN: Yes, it is. Yes, it is, and on that basis we are prepared to stand on the request for admissions.

Mr. Dunn also implicitly waived any objection to plaintiff's failure to plead an affirmative defense:

> MR. CLARK: The question of offset, of an affirmative defense, we have had that out with Judge Schwarzer when we had a pre-trial conference with him.
>
> Judge Schwarzer just brushed it aside and said, "Look, you know what the issues are here. The case is going to be tried on the issues."
>
> I didn't do anything to allege an affirmative defense after that. The discovery has all been on this issue, and I don't think there is any real point there.
>
> THE COURT: All right, ready to proceed, gentlemen?
>
> MR. DUNN: Yes.
>
> Reporter's Transcript at 8.

Later in the proceedings Mr. Dunn conceded that defendants' breach of warranty defense was no surprise to him, implying that plaintiff would suffer no prejudice if the case were allowed to proceed on that theory. R.T. at 41-43.

1976. Although there may have been some earlier informal discussions regarding the allegedly defective goods, it was not until June 1976 that defendants presented the debit memorandum to plaintiff and claimed that $261,000 worth of the goods were defective. This action cannot be considered a timely rejection of the goods. On these facts defendants must be found to have accepted the goods and thus bear the burden of showing that there was a breach of warranty.

Defendants have failed to carry this burden. The contract between the parties provided that "good" calculator circuits were to be delivered. Defendants' Exhibit 2. The contract states in relevant part:

> 7. Good circuits (i.e., circuits that conform to the contract) shall be determined by wafer probe tests performed by Seller prior to delivery in accordance with Test Procedures established by Seller and approved by Buyer pursuant to the conditions of Exhibit A. Buyer's representatives may witness all such tests. The results of said tests shall be conclusive as to the conformance of the circuits to the contract except as to latent process defects. Seller warrants that at the time of delivery the circuits shall be free from latent process defects. Seller's liability under this warranty shall be limited to, at Seller's option, the replacement of or refund of the price for defective circuits returned to Seller, transportation prepaid, within 12 months following the delivery thereof to Buyer. Seller makes no other warranties, express or implied, including any implied warranty of merchantability or fitness for purpose or against infringement, with respect to the circuits. Buyer shall bear full responsibility for the design of the circuits. Seller shall have a reasonable opportunity to cure any nonconforming tender.

Thus the contract expressly provides that the only defect for which the seller can be held liable is a latent process

defect. Defendants have failed to produce evidence to support their claim that $261,000 worth of the goods (or any of them) were subject to such a latent process defect. The only evidence to support that figure is the Monitor of Electronic Arrays Reject Analysis Reports submitted as part of Defendants' Exhibit 1. That document is merely a summary of all the rejects that occurred during the packaging process performed by Electronic Arrays. The reasons given for the rejections included bridging metal, chips and cracks, probe mark bridging, scratches, ink stains, oxide/diffusion defect, and missing metal. There is nothing in the record to suggest which, if any, of these problems were latent process defects. One of the defense witnesses, Mr. Sousan, testified that a "substantial amount" of the products delivered by Nitron did not meet the specifications regarding reverse breakdown voltage. R.T. at 32. However, there is nothing in the record which indicates the relationship between this voltage problem and the number of rejects specified in the Electronic Arrays Report. Further Mr. Sousan testified on cross-examination that wafers and dice are susceptible to malfunction after initial testing by the seller as a result of defects other than latent process defects. R.T. at 56. On this record, defendants must be found to have failed to carry their burden of showing that any specific quantity of the goods had latent process defects. Defendants' breach of warranty theory must therefore be rejected.

B. Account Stated

Defendants' second and principal theory is that plaintiff agreed that it owed Commodore the amount stated in the debit memorandum, thereby creating an enforceable account stated on accord and satisfaction. The evidence establishes that the debit memorandum was presented by defendants'

representatives to Dr. Sharif, president of Nitron, who asked them to withdraw it because if it appeared on Nitron's books it would place the company in a precarious financial position. Since Nitron was Commodore's only source of supply for these parts, it was in Commodore's interest to see that Nitron stayed in business, and Commodore therefore did withdraw the debit memorandum. It was never accepted by Nitron or posted on its books. Nor is there any other evidence that plaintiff's representatives ever agreed that any specific amount was due defendants as a result of the problems reflected in the debit memorandum.

Mr. Sousan, a former Commodore vice-president who participated in the meetings with Nitron at which the debit memorandum was discussed, was asked by plaintiff's counsel:

> Q. Did Mr. Sharif state at those meetings that McDonnell Douglas Corporation or Nitron, as the case may be, agree that Commodore was entitled to a credit of $261,000, and that they would be paid or would be credited for that amount?

Mr. Sousan replied:

> A. He did not state this in these words that you just used, Mr. Dunn.

R.T. at 51

This evidence is insufficient to sustain defendants' burden of proving that an agreement was reached. It is not bolstered by the testimony that Nitron representatives did not express disagreement with the numbers reflected in the debit memorandum. R.T. at 39, 66. In fact, Mr. Tramiel, the President of Commodore, testified that there was no discussion about how this issue would be settled in the future. R.T. at 66. Nor are the deficiencies in defendants' showing cured by Mr. Sousan's general testimony that Nitron

"requested that these debit memorandums [sic] be kept in abeyance until such time that future business based on these higher output promied [sic] to Commodore would afford Nitron to apply it as credit to Commodore." (R.T. at 37) The Court therefore finds and concludes that defendants have failed to prove the existence of an agreement entitling them to set off $261,000.

Defendants' argument that plaintiff's failure to call Dr. Sharif as a witness creates an inference that an agreement was reached on the $261,000 credit is not persuasive in view of the evidence demonstrating that no agreement was reached. In any event, such an inference, in the light of the evidence as a whole, is insufficient to sustain defendants' burden on the issue.

Defendants also object to the magistrate's finding that Commodore never returned the defective goods to Nitron and the corresponding conclusion that Commodore for this additional reason was entitled neither to a setoff nor to recovery for breach of warranty. Inasmuch as the Court has determined that defendants have failed to sustain their burden on the breach of warranty and set-off claims, it is unnecessary to reach this issue. It is also unnecessary to determine whether the contractual limitation of remedy to replacement or refund, at the seller's option, precludes defendants' claims.[3]

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3. Defendants have not objected to the finding of the magistrate that they are not entitled to any additional credit for defective goods shipped under the new contract entered into by the parties in July, 1976. They argued at trial that the new contract made Nitron explicitly liable for any defects discovered by Commodore during its testing procedures. Commodore claimed entitlement to a credit for some 15,000 dice that were discovered to be defective at a secondary testing step. The record supports the magistrate's finding that no notice was ever given to Nitron of these defects prior to trial. The new contract explicitly provides that "Nitron shall have a reasonable opportunity to cure any

Judgment will be entered for plaintiff in the amount of $432,908.36. This judgment is for "damages certain", thus qualifying for prejudgment interest under California law. Cal. Civil Code § 3287(a). That statute provides that interest begins to run from the time the liquidated amount became due. Here plaintiff sent a letter to defendant's vice president for finance on August 15, 1977, stating that four equal monthly payments would be accepted in payment of the $432,908.36 it demanded. Defendants received this letter on August 17. The time for payment thus having expired on December 17, 1977, interest will be awarded from that date.

IT IS SO ORDERED.

DATED: August 10, 1979

WILLIAM W SCHWARZER
William W Schwarzer
United States District Judge

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nonconforming tender." Defendants' Exhibit 3. Notification is a prerequisite to an opportunity to cure. Since plaintiff has not been given the contractually required opportunity for cure as to these 15,000 additional allegedly defective dice, defendants are not entitled to recover their price or to a set-off in that amount.